

Chapter 5

Organizing the Venture

By
Mrs. Kavana K. V

Introduction

- Ventures provides access to business training, capital, coaching and hands-on learning opportunities for entrepreneurs.
- The first organizing decision of an entrepreneur is the forms of legal ownership for the venture.
- It's important to know, examine, and evaluate the advantages and disadvantages of ownership ventures.

What are Legal forms?

- Legal form identifies the legal status of a legal person.
- The classification of legal forms is based on the company forms of the Trade Register(The Trade Register is a nationwide central register, which contains official information on businesses regardless of their business form.) and on the requirements of taxation legislation.(The proposed tax laws start the formal tax legislation process as a bill before it is to become law.)
- Every small business must select a legal form of ownership.
- The legal forms of enterprises and corporations are recorded in the Business Information System.

Primary factors

- The two primary factors that affects the decision to choose legal forms are:

Tax is a compulsory financial charge imposed upon a taxpayer (an individual or legal entity) by a governmental organization in order to fund various public expenditures.



Legal liability describes a situation in which a small business is held legally responsible for injuring or financially harming another party. This judgment can result in fines, penalties, or other payments.

Ways of organizing entrepreneurial venture

- The ways of organizing entrepreneurial ventures are:
 - Sole Proprietorship
 - General Partnership
 - Limited Liability Partnership
 - C Corporation
 - S Corporation
 - Limited Liability Company

Sole Proprietorship

- A **Sole Proprietorship** is a form of organization in which the owner maintains sole and complete control over the business.
- There are no legal requirements for establishing a sole proprietorship other than obtaining necessary local business licenses and permits.
- In a sole proprietorship, income and losses “pass through” to the owner.
- Liability Issues are the major concerns.



Advantages and Disadvantages of Sole Proprietorship

Advantages

- A sole proprietorship has few formalities and low organizational costs.
- Decisions are made by the owner.
- There are fewer reporting requirements for government agencies.
- Corporate "double tax" is avoided.

Disadvantages

- Compared to corporations and partnerships, sole proprietorships cannot take advantage of certain benefits afforded by the Internal Revenue Code.
- The business terminates upon the death of the owner.
- Investment capital is limited to that of the owner.
- Loans are based on the creditworthiness of the owner.

General Partnership

- A **General partnership** is a form of business organization in which two or more business owners share the management and risk of the business.
- All partners share equally in the right and responsibility to manage the business.
- Each partner is responsible for all debts and obligations of the business.
- The filings are optional and not mandatory.



Advantages and Disadvantages of General Proprietorship

Advantages

- A general partnership is a business owned by two or more people, who carry on the business as a partnership. Partnerships have specific attributes.
- All partners share equally in the right and responsibility to manage the business.
- Each partner is responsible for all debts and obligations of the business.
- The filings are optional and not mandatory.

Disadvantages

- Each partner has the power to act on behalf of the business, which requires that partners be chosen with care.
- The partnership has no continuity of life. If any partner dies or becomes incompetent, such partner's interest is dissociated from the partnership and the partnership may be dissolved and reformed.
- All partners must pay tax on their share of partnership profits, although profits may be retained in the business.

Limited liability partnership(LLP)

- LLP is a form of business organization in which there are general partner and limited liability partners.
- An LLP faces a similar tax situation as a general partnership. Income and losses “pass through” to the partners and are taxed at personal rates.
- The liability issue is a distinguishing feature of the LLP. Although at least one general partner must have unlimited liability, the limited partners are liable only up to the amount of their investment in the LLP.

Advantages and disadvantages of LLP

- The main advantage of the LLP is that is a good way for an entrepreneur to raise capital.
- The general partners have the opportunity to obtain funds without having to go through a financial institution.
- The biggest disadvantage of this form of organization is the cost and complexity of forming the LLP.
- Another disadvantage is that limited partners cannot participate in the management of the partnership without losing their liability protection.

C corporation

- C corporation is a legal business entity that is separate from its owners and managers.
- Any corporation that is taxed separately from its owners.
- The corporation functions as a distinct legal entity can make contracts, engage in business activities, own property, and of course pay taxes.

What does it take to incorporate?

Articles of incorporation typically include the following information

- The name of your company
- The purpose of your business
- The names and addresses of the incorporators
- The names and addresses of the corporation's initial officers and directors.
- The address of the corporations home office
- The capital required at the time of incorporation
- Capital stock to be authorized
- Corporate bylaws
- Corporations time horizon
- Miscellaneous information

S Corporation

- The S corporation has been the classic mechanism for getting the limited liability of a corporate structure without incurring corporate tax.
- An S corporation is not subject to income tax; rather, its shareholders are subject to tax on their pro rata shares of income based on their shareholdings.

Current criteria regarding S corporation:

- S corporation can now have as many as 75 shareholders.
- Any trust that owns shares in an S corporation can now have multiple beneficiaries rather than just one.

Limited liability company(llc)

- The LLC is a relatively new form of business organization that's another hybrid between a partnership and a corporation.
- The LLC offers the liability protection of a corporation, the tax benefits of a partnership and no restriction such as those on an S corporation.

Advantages and disadvantages of LLC

- LLC is the flexibility that it gives owners, In addition, the fact that the LLC is not constrained by the regulations on C and S corporation is an advantage.
- The absence of double taxation is an advantage of this organizing approach.
- The main drawback of this approach is the fact that its quite complex and expensive to set up.
- Legal and financial advice is an absolute necessity in forming the LLCs operating agreement, which is the document that outlines the provisions governing the way the LLC will conduct business.

Legal Issues

The four legal issues that have an impact on organizing the entrepreneurial venture are:

- Choosing a business name
- Patents
- Contracts
- Employment law

Choosing a business name, Slogan or Design

- It is an important legal issue.
- Legal problems may arise if we choose a name that another company has trademarked or
- Has registered as a corporate name with the appropriate state agency.

What is a Trademark?

- A **trademark** is a form of legal protection for a distinctive word, name, phrase, logo, symbol, design, slogan, or any combination of these elements.
- Its a good idea to do a trademark search before choosing a name, logo, slogan.
- Trademark search can be done on internet in two of the biggest trademark search companies Thomson & Thomson (www.thomson-thomson.com) and CCH Trademark Research Cooperation (www.cosearch.com).

cont

- Once you find the name ,you have to register the name with the federal government.
- Apply to the U.S.Patent and Trademark Office for a trademark name that will cover you anywhere in the United States as well as on the Internet.
- All kinds of information and forms needed for filling are available on the agency's Web site (www.uspto.gov).

What is Patent?

- A **patent** is a legal property that allows its holder to prevent others from employing this property for thier own use for a specified period of time.
- A patent protects an invention.
- Valid for upto 20 years from the date you file for the patent.

Types of Patent

- A **Utility Patent**, covers inventions that work uniquely to perform a function or use.
- If you invented a new device to administer medications, you'd apply for a utility patent. If you came up with a unique or new form, shape, or design of an existing object , you'd want to get a **Design Patent**.
- A **Plant Patent** which covers new strains of living plants such as flowers, trees, or vegetables.

Requirements

An invention must satisfy three additional requirements to be patentable.

These include:

- **Novelty** - the invention must be a new idea and physically different in at least some small way from what already exists.
- **Nonobviousness** - the invention must be a new or unexpected development, which means that it would not be obvious to someone skilled in the technology of a particular field.
- **Usefulness** – the invention must have some obvious use, or in the case of design, must be ornamental.

What is Contract?

- A **contract** is an agreement that creates legal obligations and is enforceable in a court of law.
- Organizing and then managing an ongoing entrepreneurial venture may entail executing different types of contracts.
- The commonness and potential variety of contracts that an entrepreneur may deal with means knowing something about contract law.

Essentials of a Contract

There are four essentials of a contract:

- One is **mutual assent**, which means that both parties must agree to the contract.
- Another is **consideration**, which means that both parties must do or pay something as stated in the contract.
- The third is **legality of object**, which means that the contract cannot force the parties to do something illegal.
- The final contract essential is **capacity of the parties**, which means that all parties to the contract must be legally able to perform their part of the contract.

Employment laws

- Employment laws cover hiring and firing, employee compensation and benefits, discrimination, worker's compensation, workplace health and safety, family and medical leave and other employee-employee relationships.
- New rulings and interpretations in any of these areas further complicate what you cannot do regarding any aspect of employment.
- As your venture grows and adds employees, you need to become familiar with employment law.

Other miscellaneous Legal Issues

- You may have to deal with other miscellaneous legal issues when organizing your entrepreneurial venture or while managing the ongoing venture.
- These may include sales laws, trade secrets laws, credit laws, consumer protection laws, pension, and fringe benefit laws, and antitrust laws.

Organizing

- **Organizing** is defined as the process of deciding how best to get the venture's work done by grouping organizational activities and resources within some type of organizational structure.
- An **organizational structure** is the formal framework within which work is divided, grouped and coordinated.
- A visual representation of an organization's structure is called an **organizational chart**.
- The process of developing or changing the organizational structure is called **organizational design**.

Organizational Design Decisions

- Organizational design is made to make sure that the organization's work is done efficiently and effectively.
- In case of sole proprietorship there's no need to divide, group or coordinate the work because only one person makes sure all the work is done.

Key elements of Organizational Design Decisions

- Work specialization
- Departmentalization
- Chain of command
- Span of control
- Centralization-decentralization
- Formalization

Work specialization

- It describes the degree to which work tasks are divided into separate jobs also known as **division of labour**.
- Main intention of work specialization is to divide the entire job into various steps and each step is completed by different person.
- Work specialization is important in organizing work but it shouldn't be seen as a source of endlessly increasing productivity.

Advantages and Drawbacks

EXHIBIT 5-3 Advantages and Drawbacks of Work Specialization

Advantages—Economic

- Efficient use of employee skills
- Employee skills can improve because of repetition
- Easier and less costly to train employees
- Minimizes resource waste
- Encourages development of specialized equipment and machinery

Drawbacks—Human

- Boredom
- Stress
- Fatigue
- Poor work quality
- Lower productivity
- May lead to absenteeism and turnover

Departmentalization

- It describes the basis by which specialized work tasks are grouped.

General approaches to departmentalization:

- **Job function:** It reflects each organizations unique work functions.
 - **Ex:** Front desk, Maintenance, Sales, Accounting etc.
- **Product:** Here the jobs are grouped by product line.
 - **Ex:** Tax preparation, Management consulting, etc.
- **Geography:** An organization can departmentalize based on location.
 - **Ex:** Southeast region, Mideast region etc
- **Process:** Departmentalization can also be done on the basis of different process or on the basis of how products flow through the business.
 - **Ex:** Sawing, Milling, Drilling, Assembling, Packing, Shipping etc.
- **Customer:** If there are common group of customers then customer approach is the best.
 - **Ex:** Retail customers, Wholesale customers, Education customers, etc

Chain of command

- It is the flow of commands from higher level authority to lower level.
- In an appropriate organization it is important to know who has the ultimate decision making authority, who has the authority to perform tasks and who reports to whom.
- A flexible organization does not strictly follow a formal chain of command.
- But in an empowered organization employees are free to resolve the problems and work the way they feel the best.

Span of control

- It is the structural decision made regarding the number of employees that venture's supervisors can manage effectively and efficiently.
- Wider spans are more efficient in terms of cost because fewer supervisors are needed.
- But at some point the supervisor may lose track of what's going on and employees may make costly mistakes.
- These completely depend on the skills and abilities of the supervisors and employees.

Centralization-Decentralization

- **Centralization** describes the degree to which the decision making is concentrated in the hands of a few people, usually the founder and other top executives.
- **Decentralization** describes the degree to which decision making is delegated to other organizational members.

Formalization

- It is the degree to which jobs are standardized and the extent to which employee behavior is dictated by rules and procedures.
- In an highly formalized organization, there would be explicit job description, numerous organizational rules and clearly defined procedures for work activities.
- If the formalization is low, the way employees do their jobs is fairly non structure and employees have a great deal of discretion on how they work.

Types of organizational structure.

There are two types of organizational structure.

- Mechanistic organizational structure.
- Organic organizational structure.

Mechanistic organizational structure

- High specialization.
- Rigid departmentalization.
- Clear chain of command.
- Narrow span of control.
- Centralized.
- High formalization.

Appropriate for these situations

- Cost efficiencies are critical.
- Large organization (2000+)
- Standardized produced in routine fashion.
- Relatively stable and certain external environments.

Organic organization structure

- Cross functional teams.
- Free flow of information.
- Wide span of control.
- Decentralized.
- Low formalization.

Appropriate for these situations

- Innovation is critical.
- Smaller organizations.
- Customized products produced in a flexible setting.
- Dynamic, complex and uncertain external environments.

Virtual organization

- ❑ It is a network of independent people linked by common goals and information technology.
- ❑ The benefit of virtual organization is, it is extremely fluid and flexible.
- ❑ It is only possible because of information technology.

Example:

1. Strawberry frog's company.
2. Karen Drakensberg's company.

Boundaryless organization

It was coined by an entrepreneurially oriented execution of larger and successful corporation: jack welch former chairmen of global giant.

It is one whose design is not defined by or limited to, horizontal, vertical or external boundaries imposed by a predefined stricture.

The boundary less organization seeks to eliminate the chain of command, have limitless spans of control and replace rigid department lines empowered teams.

It functions efficiently and effectively by breaking down artificial boundaries created by a fixed structural design.